

# **“THERE’S A CHANGE IN THE STATUS QUO”:<sup>1</sup> CORPORATE VEIL PIERCING IN OHIO AFTER *DOMBROSKI V. WELLPOINT***

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## **I. INTRODUCTION**

In corporate law, the most litigated issue is piercing the corporate veil.<sup>2</sup> However, despite its active use, the underlying law is also one of the least understood doctrines.<sup>3</sup> Saying something significant and universally true about the doctrine of veil piercing is similar to trying to nail ‘Jell-O’ to the wall: it is a slippery, slightly messy prospect with a small chance of getting it completely right. In 1926, Benjamin Cardozo remarked that veil piercing is “enveloped in the mists of metaphor.”<sup>4</sup> Contemporary commentators<sup>5</sup> have been less kind, often referring to legal decisions to pierce the corporate veil as “irreconcilable and not entirely

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<sup>1</sup> *Enquip Technologies Group, Inc. v. Tycon Technoglass*, No. 2008-CV-1276, 2009 WL 812155, at \*22 (Ohio 2009) (citing Gary Portnoy & Judy Hart, “According to Our New Arrivals,” theme song to Mr. Belvedere (ABC Television 1985-1990), on the album *Television’s Greatest Hits*, Vol. 6 (TVT Records 1996)).

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<sup>2</sup> Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036, 1037 (1991).

<sup>3</sup> Conducting a Westlaw survey of cases, by entering search terms “piercing the corporate veil” and “disregard! the corporate entity” returned over 8700 results compared to a search of “corporate takeover” and “hostile takeover” which netted only 1100 cases. Litigated cases may not serve as a truly representative sample of all the corporate law disputes. However, the extent to which veil piercing remains a heavy factual doctrine and therefore uncertain, contributes to the sheer number of claims brought and ultimately fought out in a courtroom. *See id.* at 1046.

<sup>4</sup> *Berkey v. Third Ave. Ry. Co.*, 244 N.Y. 84, 94 (N.Y. 1926) (Judge Cardozo explained: “The whole problem of the relation between parent and subsidiary corporations is one that is still enveloped in the mists of metaphor. Metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it.”).

<sup>5</sup> Much of this scholarly work resulted in lists of theories and factors, further complicating the application of veil piercing.

comprehensible,”<sup>6</sup> “defying any attempt at rational explanation,”<sup>7</sup> and transpiring “freakishly.”<sup>8</sup>

Generally, it is the hallmark of corporations that the corporate entity and its shareholders are separate.<sup>9</sup> As separate entities, shareholders are not liable directly for the actions of the corporation. In other words, shareholders have limited liability – the shareholder can only lose the total amount of the investment.<sup>10</sup> There is no risk of personal liability. No matter what misfortune falls on the corporation, creditors cannot use the personal capital of shareholders to satisfy the outstanding debt. The doctrine of veil piercing is an exception to the general rule of limited liability.<sup>11</sup> Veil piercing allows litigants to disregard the corporate entity to personally hold shareholders responsible for corporate debts.<sup>12</sup>

However, the exception has taken on a life of its own. The doctrine is hardly made up of solid rules or quantifiable tests which lead to easily predictable outcomes: instead, most decisions describe the outer limits of the doctrine by citing a formulaic test, followed by a laundry list of factors other courts have considered significant in one manner or another, and closing with a conclusory declaration stating the result with little explanation.<sup>13</sup> Often the results are complicated by the fact that the same details appear in both cases allowing and preventing relief “in an unpatterned mingling of relevant with neutral facts that has stymied constructive analysis.”<sup>14</sup>

The doctrine of veil piercing in Ohio is similar to other states’ veil piercing doctrine. It is a diverse array of precedents, complicated, until recently, by a rule split in the appellate districts.<sup>15</sup> In 2008, *Dombroski v.*

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<sup>6</sup> PHILIP I. BLUMBERG, THE LAW OF CORPORATE GROUPS: PROCEDURAL PROBLEMS IN THE LAW OF PARENT AND SUBSIDIARY CORPORATIONS 8 (1983).

<sup>7</sup> Jonathan M. Landers, *A Unified Approach to Parent, Subsidiary & Affiliate Questions in Bankruptcy*, 42 U. CHI. L. REV. 589, 620 (1975).

<sup>8</sup> Frank H. Easterbrook & Daniel R. Fischel, *Limited Liability & the Corporation*, 52 U. CHI. L. REV. 89, 89 (1985).

<sup>9</sup> Thompson, *supra* note 2, at 1037.

<sup>10</sup> *Id.*

<sup>11</sup> The doctrine of veil piercing can go by many names including the alter ego doctrine, piercing the corporate veil, or disregarding the corporate entity.

<sup>12</sup> MODEL BUSINESS CORPORATION ACT § 6.22(b) (2002), available at <http://www.abanet.org/buslaw/library/onlinepublications/mbca2002.pdf> (“Unless otherwise provided in the articles of incorporation, a shareholder of a corporation is not personally liable for the acts or debts of the corporation except that he may become personally liable by reason of his own act or conduct.”).

<sup>13</sup> Stephen M. Bainbridge, *Abolishing Veil Piercing*, 26 J. CORP. L. 479, 509 (2001).

<sup>14</sup> Thompson, *supra* note 2, at 1037.

<sup>15</sup> See *Dombroski v. Wellpoint, Inc.*, 895 N.E.2d 538, 543 (Ohio 2008).

*WellPoint* reached the Ohio Supreme Court, forcing a resolution of the issue and providing an opportunity for needed clarification.<sup>16</sup> The court cleared up some of the mist surrounding veil piercing, but voluntarily injected some uncertainty into limited liability. *Dombroski* bolstered limited liability by creating a stricter standard for parties seeking to pierce the corporate veil but qualified it, leaving some questions unresolved.

Corporate veil piercing is a particular concern to small business owners and entrepreneurs. Unlike other corporate law issues, veil piercing is a remedy that poses a unique danger to corporations with a small number of shareholders: the possibility of personal liability for business obligations. Being stripped of the advantages of limited liability is the small business owner's worst nightmare. It creates the possibility that the owner will not only lose his or her sole source of livelihood, but also the home and other personal assets.

This Note evaluates the evolution of the doctrine of veil piercing in Ohio and its recent trends. Part II describes limited liability and the theoretical foundations for veil piercing and explains why limited liability is the default rule for corporations. Also, Part II details the typical tests associated with veil piercing and where those tests are most consistent with the theory of limited liability. Part III provides an overview of veil piercing in Ohio, including the recent appellate district split and the Ohio Supreme Court's decision in *Dombroski*. Part IV articulates how *Dombroski* impacted corporate law in Ohio by providing more security for corporations while adding a dash of uncertainty. The final part offers a conclusion as to the state of corporate veil piercing in Ohio as well as constructive thoughts on prospective business organization for practitioners.

## II. PIERCING THE CORPORATE VEIL: WHY HAVE LIMITED LIABILITY?

One of the basic advantages of the corporate form is the ability to limit the personal liability of the owners of a business.<sup>17</sup> A plaintiff cannot directly sue an individual shareholder for the tortious activities or debts of the business organization.<sup>18</sup> However, when certain requirements are met, it is possible for a party in a lawsuit to dispense with the corporate entity and allow the creditor to directly seek debt satisfaction from the shareholders of

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<sup>16</sup> *Id.*

<sup>17</sup> Bainbridge, *supra* note 13, at 480.

<sup>18</sup> *Id.*

a corporation.<sup>19</sup> When a party successfully holds the shareholders liable, it has pierced the corporate veil.

Veil piercing as an equitable remedy has received little academic scrutiny as a general matter. Part of the reason behind the lack of interest is the doctrine's general unpredictability. Rather than creating a system of predictable outcomes where firms are able to assess risk and properly allocate resources, veil piercing is perceived to be a virtual turkey shoot of factors and variables.<sup>20</sup> Businesses and legal practitioners are often left to ponder the effectiveness of their risk allocation because the true test of a corporation's limited liability occurs in the courtroom. The lack of strict standards creates substantial costs to businesses and society as a whole as firms engage in risk allocation that may be ultimately futile, as well as wasting time, resources, and limiting the socially beneficial risks that firms are willing to take.<sup>21</sup>

Veil piercing is an exception to limited liability. Understanding this exception to limited liability requires comprehending why limited liability is the default rule. The theory behind limited liability informs the debate about the application of veil piercing and demonstrates which cases are outliers. Thorough theoretical knowledge helps cut through the misty judicial language in veil piercing cases to predict when a court is willing to disregard the corporate entity.

#### *A. The Public Policy of Limited Liability: Limiting Costs*

Limited liability as an economic model creates the most efficient ordering of business relationships.<sup>22</sup> The contractarian model views the corporation as a nexus or web of contracts between the parties involved in

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<sup>19</sup> Generally to pierce the corporation's veil, a party must meet two elements: first, the party must demonstrate control of the corporation. This first step is often called the alter ego test since it attempts to demonstrate that the corporation is merely a facade for the individual shareholder. The second step is articulated in a number of different ways but usually requires some fraud, misrepresentation, or – in more creditor-friendly states – the existence of unfairness. This note focuses on the second step of the test. *See, e.g.,* *Zaist v. Olson*, 227 A.2d 552, 558 (Conn. 1967).

<sup>20</sup> Often when a judge is faced with piercing the corporate veil, the primary focus of inquiry is on the particular parties involved and the fairness of the outcome. As a result, the judge often devalues the abstract societal value of limited liability for corporate shareholders. Bainbridge, *supra* note 13, at 481.

<sup>21</sup> Bainbridge, *supra* note 13, at 481.

<sup>22</sup> In 1918, Columbia University President Nicholas Murray remarked "I weigh my words when I say that in my judgment, the limited liability of corporations is the greatest single discovery of modern times . . . Even steam and electricity are far less important than the limited liability corporation, and they would be reduced to comparative impotence without it." Williams P. Hackney & Tracey G. Benson, *Shareholder Liability for Inadequate Capital*, 43 U. PITT. L. REV. 837, 841 (1982).

creating the corporation.<sup>23</sup> Essentially the corporation is not an entity, but a long-term contract between various inputs.<sup>24</sup> This web of relationships created through explicit and implicit contracts between constituencies makes up the corporation. For example, the shareholders of a corporation provide equity capital and accept some risk of loss. The creditors provide debt capital. Employees provide labor.<sup>25</sup> These relationships make up the legal fiction of the corporation.

Corporate law is made up of default rules.<sup>26</sup> These rules are standard because presumably most parties would contractually choose them if the parties were to negotiate terms.<sup>27</sup> Therefore, the standards that satisfy the requirements of most parties are majoritarian defaults.<sup>28</sup> Parties are free to deviate from the majoritarian default rules when the rules are not ideal for obtaining their objectives but most parties are allowed to reduce transactional costs by selecting the default rule.<sup>29</sup> Under the contractual model, the primary guiding principal for rule formation is minimizing

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<sup>23</sup> Bainbridge, *supra* note 13, at 485. The contractarian model actually post-dates limited liability, but over the last few decades has become the leading theory. There are a number of other theoretical models. See, e.g., Joel Seligman, *Foreword to PROGRESSIVE CORPORATE LAW ix* (Lawrence E. Mitchell ed., 1995); William T. Allen, *Contracts and Communities in Corporation Law*, 50 WASH. & LEE L. REV. 1395, 1399 (1993); Brian R. Cheffins, *Using Theory of Study Law: a Company Law Perspective*, 58 CAMBRIDGE L.J. 197, 209 (1999). Two such models are the agency model and the concession model. Concession theory proposes corporations are the product of the state, not private enterprises. Since originally corporations were created through specific legislative enactments and are still required by state law to file for incorporation, some believed corporations were essentially the product of the state. Larry E. Ribstein, *Limited Liabilities and Theories of the Corporation*, 50 MD. L. REV. 80, 85-91 (1991). See also T. of Dartmouth Coll. v. Woodward, 17 U.S. 518 (1819). As essentially a state subsidized entity, limited liability was considered a privilege the state could revoke. Bainbridge, *supra* note 13, at 496. However, the last fifty years had essentially debunked the theory by pointing to the social benefits reaped through limited liability. *Id.* at 495. See also HERBERT HOVENKAMP, *ENTERPRISE AND AMERICAN LAW: 1836-1937* at 54 (1991). The agency theory which holds shareholders liable as the principal for the actions of its agent, the corporation. See *Walkovsky v. Carlton*, 223 N.E.2d 6 (N.Y. 1966). But generally, a corporation is not considered the agent of its shareholders.

<sup>24</sup> Bainbridge, *supra* note 13, at 485.

<sup>25</sup> *Id.*

<sup>26</sup> *Id.* While corporate law is made up of some default rules, there are some that are simply rules which parties cannot contract around.

<sup>27</sup> Bainbridge, *supra* note 13, at 486.

<sup>28</sup> *Id.* The idea behind default rules is to minimize transactional costs by choosing the most widely useable rule which parties can select without incurring the costs of negotiating for a different standard.

<sup>29</sup> *Id.*

transactional costs.<sup>30</sup> If the goal is cost minimization, parties should be free to choose whatever organization best facilitates that objective.

Limited liability is simply one of the default terms of the corporate contract.<sup>31</sup> For the majority of parties and situations, limited liability is the most economically efficient form. As a result, it would be the bargained for rule in nearly every context – for the shareholder, director, officer, and even the creditor. Systematically considering the perspective of shareholders and creditors in both public and closely held corporations will illustrate that limited liability would be the bargained for rule because it is more economically sound.

### *1. Limited Liability as the Default Rule in Public Corporations*

Limited liability of the tort and contract creditors of a public corporation is the easiest to justify. Both shareholders and creditors would prefer a structure of limited liability.<sup>32</sup> It would be easy to conclude that shareholders would negotiate for a rule of limited liability because out of a desire to avoid personal liability. But assuming shareholders would choose limited liability because of a fear of personal liability is overly simplistic. Rather, control and costs are the driving factors behind shareholders' preference for limited liability.

If the security of limited liability was the sole reason the shareholder preferred it, then all business forms would limit the financial exposure of its members.<sup>33</sup> Consider the liability of general partners. It seems reasonable to assume that if partners could choose, they would select a rule of limited liability to insulate themselves from the risks of less prudent partners or reckless employees. But, their ability to directly participate and control the firm mitigates the risk. Under the Uniformed Partnership Act (UPA) of 1914, each partner is jointly and severally liable for the other partners' actions within the scope of the partnership, whether tort or contract.<sup>34</sup> Similarly, the partners are jointly liable for all other partnership debts.<sup>35</sup> The Revised Uniform Partnership Act (RUPA) is similar. Under the RUPA, partners are jointly and severally liable for both

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<sup>30</sup> Bainbridge, *supra* note 13, at 485-86.

<sup>31</sup> *Id.* at 486.

<sup>32</sup> See Bainbridge, *supra* note 13, at 488-506.

<sup>33</sup> Currently, limited liability is not only an aspect of corporations. Many states have enacted other business forms which also provide limited liability. Every state except Vermont and Wyoming has limited liability partnership laws. CARL S. BISHOP & DANIEL S. KLIENBURGER, LTD. LIAB. CO.: TAX AND BUSINESS LAW, LLC ¶ 15.01 (West 2009). See Rev. Ltd. Liab. Co. Act (2006); UNIF. LTD. P'SHIP ACT (2001).

<sup>34</sup> UNIF. P'SHIP ACT § 15(a) (1914).

<sup>35</sup> UNIF. P'SHIP ACT § 15(b) (1914).

kinds of debts.<sup>36</sup> In either case, the partners bear a tremendous burden: the risk of personal liability beyond the assets invested in the firm for the actions of fellow partners or agents.<sup>37</sup>

Shareholders on the other hand want to limit personal exposure because of the costs involved in unlimited liability.<sup>38</sup> In a world of unlimited liability, shareholders would exercise more direct control over the corporation's operations.<sup>39</sup> If a shareholder's personal assets could satisfy corporate debts, the shareholders would demand a more active role in directing the firm's operations to accompany their risk.<sup>40</sup> Shareholder control comes at a tremendous cost to management. The management of a company would need to provide information and facilitate active participation by shareholders.<sup>41</sup> In the modern public corporation, the participation of individual shareholders in the management of the company would be bedlam. Imagine thousands of individuals in a major corporation attempting to exercise information or control rights. To say such activity would interfere with efficient centralized management of the corporation would be an understatement.

In addition to these management costs, shareholders would assume tremendous monitoring costs if there was joint and several liability.<sup>42</sup> Shareholders would need to both monitor the management of the firm and other shareholders' creditworthiness.<sup>43</sup> Most shareholders are rationally apathetic because of a pre-occupation with jobs, family, or other matters.<sup>44</sup>

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<sup>36</sup> REVISED UNIF. P'SHIP ACT § 306 (1996), available at

<http://www.law.upenn.edu/bll/archives/ulc/fnact99/1990s/upa97fa.pdf>.

<sup>37</sup> Professor Larry Ribstein has argued the partnership form of organization has survived "because of regulation and tax law, and not because of the preferences of individual contracting parties." Robert W. Hamilton & Larry E. Ribstein, *Limited Liability and the Real World*, 54 WASH. & LEE L. REV. 687, 693 (1997).

<sup>38</sup> Bainbridge, *supra* note 13, at 489-91.

<sup>39</sup> Partners, however, have both unlimited liability and the control to protect it. Each partner "is given an equal voice in decisions that expose him or her to potentially unlimited personal liability." Bainbridge, *supra* note 13, at 490.

<sup>40</sup> Bainbridge, *supra* note 13, at 500.

<sup>41</sup> Harry G. Hutchinson & R. Sean Alley, *The High Costs of Shareholder Participation*, 11 U. PA. J. BUS. L. 941, 949 (2009) (noting that "[r]ational shareholders demand participation in their investments only when the benefits of doing so (in the broadest sense) are greater than the costs.").

<sup>42</sup> Bainbridge, *supra* note 13, at 490.

<sup>43</sup> Paul Halpern et al., *An Economic Analysis of Limited Liability in Corporation Law*, 30 U. TORONTO L.J. 117, 136 (1980).

<sup>44</sup> See ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* 81 (1932); Bernard S. Black, *Shareholder Passivity*

But the monitoring necessary under unlimited liability would demand much more time and effort, essentially turning investing itself into a full time job or severely limiting the number of investments a shareholder could make.<sup>45</sup> In either case, with a rule of unlimited liability, the shareholder's ability to diversify away some risks would be damaged, if not eliminated. However, under limited liability, shareholders are able to diversify stock portfolios and refrain from monitoring. If one investment tanks, the shareholder still has other investments and will only lose a small portion of his or her capital value.<sup>46</sup>

On a superficial level, it seems ridiculous to argue contractual or tort creditors would choose limited liability. Limited liability would effectively limit the collection of an outstanding debt to corporate assets. Once those assets are exhausted, the creditors would be stuck without recourse.<sup>47</sup> If nothing else, creditors would want the option of securing financial obligations using personal assets and capital of shareholders.<sup>48</sup> But, balancing the advantages of unlimited liability against the cost of enforcement and the detriment to society indicates that even creditors prefer that shareholders have limited liability.

First, creditors would have insurmountable procedural problems with enforcing unlimited liability. Initially, creditors would need to obtain personal jurisdiction over shareholders who might reside out of state. However, it seems doubtful that they could do so constitutionally.<sup>49</sup> Since

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*Reexamined*, 89 MICH. L. REV. 520, 527 (1990) (noting the view that "[c]ollective action problems make shareholder passivity inevitable").

<sup>45</sup> Bainbridge, *supra* note 13, at 491.

<sup>46</sup> *Id.* The prospect of unlimited liability also creates a free riding problem between shareholders. Most shareholders would benefit from the monitoring of a few shareholders but would not need to incur the costs themselves. ROBERT COOTER & THOMAS ULEN, *LAW AND ECONOMICS* 101 (2d. ed. 1997). They could obtain the benefit from the collective activity of the other shareholders. *Id.* However, the incentives to free ride will be great since most of the gains of monitoring will go to both monitoring and non-monitoring shareholders. Stephen M. Bainbridge, *Redirecting State Takeover Laws at Proxy Contests*, 1992 WIS. L. REV. 1071, 1081-83 (1992). Since these incentives are high, there may be too much free riding. The result would be inadequate monitoring and eventually losses from ineffective supervision. Therefore, because of the costs to the firm in shareholder management, the costs of monitoring to shareholders, and the risks of rendering monitoring ineffective because of free riding, shareholders prefer limited liability over unlimited liability.

<sup>47</sup> Bainbridge, *supra* note 13, at 492.

<sup>48</sup> *Id.*

<sup>49</sup> Janet Cooper Alexander, *Unlimited Shareholder Liability Through a Procedural Lens*, 106 HARV. L. REV. 387, 389-99 (1992). However as an alternative, if a firm enters bankruptcy national service of process is available since there is nationwide



*International Shoe*, a defendant must have minimum contacts with the jurisdiction.<sup>50</sup> However, in *Shaffer v. Heitner*, the Supreme Court held ownership of stock shares did not create minimum contacts in the state where the company was incorporated.<sup>51</sup> It seems implausible that a creditor could sustain jurisdiction against a shareholder based solely on stock ownership. This would limit the pool of shareholders and shareholder assets to a small group of in-state shareholders, none of who may have substantial assets, individually or collectively.

Assuming creditors could locate sufficient shareholders that a court would have personal jurisdiction over, the creditors would need to determine a choice of law question: whether the law of the state of incorporation governs such a suit.<sup>52</sup> Any question about the rights or obligations of shareholders is necessarily a question of state law.<sup>53</sup> These questions are generally answered under the corporate law for the state of incorporation.<sup>54</sup> However, if a state would permit unlimited liability and a creditor was to sue a shareholder, presumably the state law of the incorporating state would control.<sup>55</sup> States permitting unlimited liability would be a serious competitive disadvantage protecting their corporate law franchise. Few, if any, corporations would incorporate in a jurisdiction permitting shareholder liability. As a result, any state would be hesitant to permit unlimited liability on its own.<sup>56</sup>

Even ignoring these procedural issues, creditors will be obliged to monitor the creditworthiness of all (or at least the wealthiest) shareholders.<sup>57</sup> Since the shareholders are the ultimate source of funds in an unlimited liability world, creditors would need assurance that the assets of

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jurisdiction. See LYNN LOPUCKI, STRATEGIES FOR CREDITORS IN BANKRUPTCY PROCEEDINGS § 3.03[D] (3d ed. 1997).

<sup>50</sup> *Int'l Shoe Co. v. Washington*, 326 U.S. 310, 316 (1945).

<sup>51</sup> *Shaffer v. Heitner*, 433 U.S. 186, 213 (1977).

<sup>52</sup> *Id.* Some states might obtain a competitive advantage over other states by creating a default rule of limited liability, which might render the debate moot.

<sup>53</sup> Alexander, *supra* note 49, at 410.

<sup>54</sup> *Id.* This concept is generally known as the internal affairs doctrine. The internal affairs doctrine states that in the interest of predictable and uniform application of the law, the state of incorporation has the closest connection with the issues. Therefore, the law of the state of incorporation should govern.

<sup>55</sup> *Id.* at 413.

<sup>56</sup> Creation of such a state law would also create basic fairness and possibly constitutional problems. Effectively a state would be exercising its legal power through legislation over people with a limited relationship with the state, and no ability to influence policy. *Id.* at 413.

<sup>57</sup> Halpern, *supra* note 43, at 134.

shareholders surpass any expected claim.<sup>58</sup> Otherwise, the creditor would run the risk of lending to a corporation with no tangible security in shareholder capital or assets. Though the right to sue shareholders would exist, it would be functionally useless if the shareholders had no assets. The costs associated with monitoring shareholder credit would be expensive, especially when compared to monitoring the corporation's credit.<sup>59</sup> Creditors of large corporations would be willing to accept limited liability for shareholders.<sup>60</sup> There are some benefits to permitting liability of shareholders, but the procedural hurdles and the monitoring costs to creditors demonstrates limited liability is preferable to creditors. Placing the two on balance, creditors are unwilling to shoulder the additional burdens associated with unlimited liability.<sup>61</sup>

Finally, from a policy perspective limited liability is inefficient since it merely shifts costs rather than reducing them.<sup>62</sup> If shareholders were held jointly and severally liability, creditors would presumably target the largest shareholders with the most assets to satisfy any outstanding debt. These shareholders would seek contribution from other shareholders through the justice system. Enforcement costs therefore shift from the creditors to the largest shareholders and society as a whole.<sup>63</sup> Instead of creating efficiency, liability would effectively create a chain reaction of lawsuits where the wealthiest shareholders seek contributions from the other shareholders. These shareholders then in turn will take other shareholders into court in a web of suits seeking contribution. The costs to society to enforce unlimited liability would be prohibitively expensive since courts would be burdened by a line of shareholders seeking contribution.<sup>64</sup>

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<sup>58</sup> *Id.* The cost of monitoring creditworthiness is continuous. While an initial credit check provides a snapshot of the assets available to satisfy default, it is the financial position of the shareholders at the time of default that the creditor is most interested in monitoring. Creditors can only collect from shareholders in the amount possessed at the time breach of contract occurs. As a result, continual and persistent monitoring is necessary, which in turn increases costs. These information costs are shifted back to the owners of the company through a higher interest rate for credit.

<sup>59</sup> Bainbridge, *supra* note 13, at 493.

<sup>60</sup> *Id.*

<sup>61</sup> *Id.*

<sup>62</sup> *Id.*

<sup>63</sup> *Id.* Joint and several liability also creates a basic fairness problem: the most wealthy shareholder (regardless of the number of shares possessed) will be targeted by creditors.

<sup>64</sup> In addition, joint and several liability sends ripple effects into secondary markets significantly influencing the ability to sell stock by decreasing its transferability. The actual value of the stock would need to include the assets of the stockholders who owned the shares. As a result, shares would not only reflect the value of cash

Similar to contract creditors, involuntary tort creditors would likely prefer limited liability because the alternative makes it *more* difficult for creditors to collect against corporations. Limited liability encourages equity investment in corporations.<sup>65</sup> This means corporations have a pool of capital available to satisfy all debt obligations. By promoting investment, limited liability creates a larger pool of capital that tort creditors can draw from if they are successful.<sup>66</sup> Tort creditors want the corporation to have a large equity cushion. If the corporation would declare bankruptcy, the tort creditor's claim would be subordinated to the claims of secured creditors and shared pro rata with other general creditors.<sup>67</sup> Or if there was unlimited liability, fewer people would invest and fewer equity funds would be available to satisfy the claim because of the lower position of the tort creditors. Tort creditors would likely prefer limited liability because the equity pool is larger and because of the incentive to invest.<sup>68</sup>

In conclusion, both the contract and the tort creditors of large corporations should prefer limited liability. Limited liability eliminates enforcement and monitoring costs and the procedural issues associated with enforcing a judgment against out of state shareholders. It creates a deeper

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flow to the company, but would depend on the owner's ability to pay debts. The effect would be non-fungible shares. Bainbridge, *supra* note 13, at 493.

<sup>65</sup> Even the most staunch critics of limited liability admit that allowing unlimited liability of shareholders would increase the costs of equity investment. Henry Hansman & Reinier Kraakmann, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879, 1903 (1991) ("Indeed, the purpose of unlimited liability is to make share prices reflect tort costs."). While the rational investor might not care, loss averse investors (which constitute most people) will overemphasize the rises of an investment under unlimited liability. Bainbridge, *supra* note 13, at 498.

<sup>66</sup> Bainbridge, *supra* note 13, at 498. While Hansman and Kraakman do point out unlimited liability would increase the cost of equity investment since share prices would reflect tort risk, they contend there would not be an exodus from the equity market. However, behavioral economics shows that often when individuals make investments, the behavior is often framed in terms of potential losses, not gains. So the fear of losing a certain sum of money outweighs the pleasures of receiving the same amount because most people are loss averse. Though this activity is inherently irrational, investors will tend not to invest in equity markets.

<sup>67</sup> *Id.*

<sup>68</sup> Unlimited liability creates other hurdles for any creditor. The usual constitutional and procedural hurdles for any creditor also pose problems for involuntary creditors. In addition, for a shareholder to be personally liable a court must define when liability attaches: when the claim is filed, when the injury occurs, or at the time of judgment. None of these options is particularly easy to administer and often incentives dumping stock by startled shareholders. See Bainbridge, *supra* note 13, at 497.

pocket for tort creditors to satisfy their claim. In addition, the shareholders themselves can avoid the costs of monitoring the corporation's management and one another. A default rule of limited liability is therefore the most beneficial for all parties involved. Since limited liability is the most rational rule of parties, it has become the default for contract creditors.

## 2. *Limited Liability as the Default in Closely Held Corporations*

A default rule of limited liability for the closely held corporation is more difficult to justify. Since the shareholders and managers are the same, there is a greater possibility of the corporations externalizing risk onto its creditors.<sup>69</sup> There are fewer costs to creditors for collecting a claim and monitoring corporate constituencies.<sup>70</sup> The choice of law and personal jurisdiction issues are less problematic because the shareholder and corporation are in the same state.<sup>71</sup> Finally, unlike public corporations, many contract creditors require shareholders of a closely held corporation to personally guarantee the loan by negotiating around the default rule.<sup>72</sup> Since many creditors bargain around the rule, it seems counterintuitive to require parties to incur expenses bargaining around the default rule. But since the creditor is the cheapest cost avoider, the burden of bargaining is placed with him or her.<sup>73</sup>

As the cheapest cost avoider, the contract creditor is in the best position to determine if the added protection of the shareholder's personal

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<sup>69</sup> FRANK H. EASTERBROOK & DANIEL R. FISCHER, *THE ECONOMIC STRUCTURE OF CORPORATE LAW* 56 (1991). Compare the close corporation to the public corporation where ownership and control are separate. The diversified shareholders cannot force the directors or officers to take any action, particularly actions which risk adverse managers are hesitant to take. Bainbridge, *supra* note 13, at 501.

<sup>70</sup> *Id.*

<sup>71</sup> *Id.* Bringing a claim against a closely held corporation or its shareholders generally presents few legal procedural issues. Since the corporation and its limited number of shareholders are nearly one in the same, the shareholders are almost always found in the same jurisdiction. As a result, the personal jurisdiction and choice of law issues become moot.

<sup>72</sup> *Id.* In other words, the creditor requires that the shareholder provide his or her own personal assets as security, negating the rule of limited liability.

<sup>73</sup> There is also a problem with defining a closely held corporation which makes the blanket rule more appealing. See Bainbridge, *supra* note 13, at 501. When there are a handful of shareholders, unlimited liability makes sense as a default rule, but it is difficult to determine when there are enough shareholders to negate the need for limited liability. Randomly selecting a critical mass of shareholders which is sufficient limited liability is non-sensical and arbitrary.

assets is necessary to provide security for the loan.<sup>74</sup> Limited liability then serves as a penalty on the creditor. Without contracting around the default rule of limited liability, creditors might suffer a loss if the firm becomes insolvent. Their ability to recover damages is limited to corporate assets that might prove insufficient.<sup>75</sup> But even if creditors are the cheapest cost avoider, making them bear the transactional costs to bargain around the default rule of limited liability seems unfair.<sup>76</sup> After all, if the majority of them would choose unlimited liability, the most efficient rule would eliminate transaction costs incurred by the creditor contracting around the debt. In this situation, limited liability acts as a penalty default. But imposing the penalty on creditors is the most efficient outcome, despite the transactional costs. Limited liability forces creditors to bargain because the costs to the judicial process are greater than the costs of forcing creditors to bargain. The overall costs of creating a penalty default are less than creating a rule of unlimited liability and forcing courts to determine *ex post* what the parties actually intended.<sup>77</sup> Since it is less costly to force the cheapest cost avoider creditor to bargain out of limited liability, it remains the default rule.<sup>78</sup>

Limited liability for the tort creditors of shareholders of closely held corporations is the most difficult to justify which is why many commentators have proposed abolishing it.<sup>79</sup> Shareholders are actively involved in the business and would have low monitoring costs over

<sup>74</sup> GUIDO CALABRESI, THE COSTS OF ACCIDENTS 135 (1970) (discussing "cheaper cost avoider" concept in tort context); cf. COOTER & ULEN, *supra* note 46, at 242 (discussing concept of "lowest-cost risk-bearer" in contract context).

<sup>75</sup> Forcing creditors to bear the costs to contract around the default rule seems unfair. Penalty defaults "are most appropriate where it is more costly for courts to determine what the parties would have wanted than for the parties to bargain *ex ante*." Bainbridge, *supra* note 13, at 502.

<sup>76</sup> COOTER & ULEN, *supra* note 46, at 242.

<sup>77</sup> Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 91 (1989).

<sup>78</sup> The exception to this explanation is where the shareholder misrepresents the assets of the corporation to the creditor. When a shareholder misrepresents, the creditor does not know of the need to bargain for a personal assurance from the shareholder. However, misrepresentation is one of the classic justifications for veil piercing. See *Perpetual Real Est. Servs., Inc. v. Michaelson Props., Inc.*, 974 F.2d 500, 545 (4th Cir. 1992). Under the MBCA, if a controlling shareholder misleads the creditor there may be no need to make a veil piercing claim. 1 MODEL BUS. CORP. ACT. ANN. § 6.22(b) (3d ed. Supp. 1997) (a shareholder "may become personally liable by reason of this own acts or conduct.").

<sup>79</sup> Hansmann & Kraakmann, *supra* note 65, at 1916-23; see also David W. Leebron, *Limited Liability, Tort Victims, and Creditors*, 91 COLUM. L. REV. 1565, 1613-23 (1991).

management – since they *are* effectively the management. The shareholder is also often the cheapest cost avoider and could exercise control to assure adequate insurance or monitoring employees. The creditor also will incur few enforcement costs against a limited number of shareholders.

However, limited liability remains the default rule because it is socially undesirable for the shareholders in a close corporation to internalize all the risks created by the firm.<sup>80</sup> Shareholders of close corporations do not escape under limited liability.<sup>81</sup> If a tort claim is brought, the shareholder stands the possibility of losing his or her job if the company folds in addition to whatever personal assets the shareholder invested in the corporation.<sup>82</sup> But more importantly, tort creditors free ride on the monitoring from contract creditors.<sup>83</sup> Contract creditors usually require the corporation to have a pool of unencumbered assets.<sup>84</sup> Tort creditors therefore receive the benefit of contract creditors' monitoring, assuring there is at least some pool of assets for the creditor to draw upon.<sup>85</sup> As a result, social policy does not require shareholders to internalize tort risk by creating a default rule of unlimited liability.

#### A. *The Exception to Limited Liability: Piercing the Veil*

On an abstract level, veil piercing should coincide with the weakest justifications for limited liability. Ideally, these are the places where there is the greatest risk of the corporation externalizing risk and the lowest costs of enforcement. In practice, the court should ask whether the shareholder should be forced to internalize the risks that he or she has externalized by balancing the need to compensate victims, capital formation, and the

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<sup>80</sup> There is also the same line drawing problem that plagues contract creditors of close corporations.

<sup>81</sup> It is also important to note the small number of creditors in the involuntary tort category. It is fair to assume most corporations do not engage in excessive amounts of tort risk. As economist Michael Dooley has pointed out, corporations, "unless we are nearing Doomsday – produce goods and services that are entirely benign from a health standpoint and restrict their 'risk taking' to the financial variety." MICHAEL P. DOOLEY, *FUNDAMENTALS OF CORPORATION LAW* 56 (1995). The radical proposal of dispensing with limited liability makes even less sense when it is pointed out how few people are affected. Bainbridge, *supra* note 13, at 500 n.101.

<sup>82</sup> Bainbridge, *supra* note 13, at 504.

<sup>83</sup> *Id.*

<sup>84</sup> *Id.*

<sup>85</sup> Empirical evidence supports the conclusion that despite the attractiveness of unlimited liability for shareholders when there is a tort, such claims are rarely successful. Instead, the most successful veil piercing claims are predominantly by contract creditors. Thompson, *supra* note 2, at 1058 (registering a success rate of thirty-one percent for tort creditors).

development and growth of the economy.<sup>86</sup> But many commentators have pointed out the uncertainty of piercing cases.<sup>87</sup> Veil piercing has a number of cases which are outliers and do not conform to the theory of veil piercing. Some of these decisions are explainable as the result of the remedy's equitable nature and the number of factors that courts have indicated are relevant.<sup>88</sup> Some improper applications are expected. Veil piercing is highly contextual – and sometimes downright unpredictable – but looking at cases, a main body of decisions illustrates the situation where veil piercing is nearly a guarantee.<sup>89</sup>

The contractarian theory of limited liability indicates there are some instances when a corporation's veil should be pierced, primarily when there is a closely held corporation and there is misrepresentation or fraud.<sup>90</sup> In a closely held corporation, the shareholders are the managers, unlike the public corporation where there is a separation of control and ownership.<sup>91</sup> Thus in close corporation, there are greater incentives to externalize risk because the managers will directly benefit from the gains of risky behavior as shareholders.<sup>92</sup> Similarly, fraud or misrepresentation by the shareholder deceives the creditor into believing no personal assurance is needed and therefore no bargaining around the default rule. In other words, the creditor does not know that he or she needs protection from the default standard. Therefore, piercing a corporation's veil is consistent with limited liability

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<sup>86</sup> Bainbridge, *supra* note 13, at 506.

<sup>87</sup> See *supra* notes 6-8.

<sup>88</sup> Courts have indicated that the following factors are relevant to veil piercing cases: undercapitalization; misrepresentation; failure to follow corporate formalities; overlap of corporate records; functions or personnel; misrepresentation; shareholder domination; intertwining and lack of substantive separation; use of the terms 'alter ego' and 'instrumentality'; fairness; assumption of risk; refusal to let a corporation pierce itself; statutory policy. Thompson, *supra* note 2, at 1044.

<sup>89</sup> Thompson, *supra* note 2, at 1038-39. The rationale for piercing is more effective in contract claims than torts, leading to more success for tort claims. Most formalities of the rule demonstrate that the two prongs must be met for a corporation's veil to be pierced: control and fraud or injustice. The second element is easier to prove for contract creditors where there is often concrete evidence of fraud or misrepresentation.

<sup>90</sup> Bainbridge, *supra* note 13, at 503 n.114.

<sup>91</sup> *Id.* at 501.

<sup>92</sup> Sometimes the very purpose of incorporation can be to externalize risk. For example, in *Walkovsky*, the shareholder could have chosen to organize his taxi company as a sole proprietorship, partnership, or corporation. However, he chose to incorporate each individual taxi cab in order to avoid personal liability. *Walkovsky v. Carlton*, 223 N.E.2d 6, 6-7 (N.Y. 1966)

theory when a closely held corporation's shareholders engage in misrepresentation or fraud deceiving creditors.<sup>93</sup>

Most courts have indicated that numerous factors are relevant when deciding to disregard the corporate entity, including: undercapitalization; misrepresentation; failure to follow corporate formalities; overlap of corporate records; functions or personnel; shareholder domination; intertwining and lack of substantive separation; conclusory use of the terms 'alter ego' and 'instrumentality'; fairness; assumption of risk; refusal to let a corporation pierce itself; and statutory policy.<sup>94</sup> In a typical formulation, these factors are grouped into a two pronged 'instrumentality' test requiring first, domination or control of the corporation and second, some sort of fraud or injustice which violates the creditor's rights.<sup>95</sup> In practice, these two steps cover most of the situations where the justifications for limited liability are weakest.

First, courts typically find control of a corporation when there is a shareholder who dominates the corporation to the extent that the person and the corporation are one in the same.<sup>96</sup> There are no corporate ends beyond the controlling shareholder's goals. The corporation is a facade or dummy for an individual acting in his or her own benefit. Often this is exemplified by co-mingling corporate and personal assets or the failure to observe corporate formalities.<sup>97</sup> Requiring control or domination is consistent with the underpinning of limited liability.<sup>98</sup> The control requirement excludes large public corporations. Limited liability for public corporations with many shareholders encourages the transferability of stock and diversification as well as negates the need for expending monitoring costs.<sup>99</sup> However, when there is a close corporation, these concerns are less prominent. Managers of close corporations with few shareholders have the

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<sup>93</sup> In comparison, perhaps the thinnest rationalization for limited liability is the tort creditor because of the inability of creditors to bargain around the rule. Bainbridge, *supra* note 13, at 505 (citing Thompson, *supra* note 2, at 1058). However, tort creditors have more difficulty in piercing the corporate veil. Tort creditors are only successful about a third of the time. Bainbridge, *supra* note 13, at 505.

<sup>94</sup> Thompson, *supra* note 2, at 1044.

<sup>95</sup> Bainbridge, *supra* note 13, at 507-08. Some courts have sanctioned an agency view of the corporation and its shareholders by permitting veil piercing when there is only control of the corporation. See *Walkovsky*, 223 N.E.2d at 6.

<sup>96</sup> This first part of the test is analogous to the alter ego step of the *Belvedere* veil piercing test in Ohio. See *Belvedere Condominium Unit Owners' Ass'n. v. R.E. Roark Cos., Inc.*, 617 N.E.2d 1075, 1086 (Ohio 1993).

<sup>97</sup> See *Sea-Land Services, Inc. v. Pepper Source*, 993 F.2d 1309, 1312 (7th Cir. 1991) (court noting co-mingling of corporate assets by the single shareholder of a corporation and failure to observe formalities indicated that the shareholder-defendant dominated the corporation).

<sup>98</sup> Sometimes undercapitalization is considered a factor in demonstrating control. See *McCallum Family LLC v. Winger*, 221 P.3d 69, 74 (Colo. App. 2009).

<sup>99</sup> Bainbridge, *supra* note 13, at 501.



greatest incentives to engage in risky behavior.<sup>100</sup> When a closely held corporation is dominated by a single shareholder, the most significant limited liability concerns are triggered because shareholders have the greatest incentives to externalize risk.<sup>101</sup> This theory is supported by empirical evidence: public corporations are never pierced.<sup>102</sup> In Professor Richard Thompson's survey of two thousand veil piercing cases, not a single public corporation's veil was pierced.<sup>103</sup> Thompson's research indicates that when a court points out a lack of separation between the individual and corporation, intertwining, or use of the term "dummy," the court pierces the veil in over eighty-five percent of cases.<sup>104</sup> When the court notes the absence of domination or control, the veil is not pierced in over ninety-eight percent of cases.<sup>105</sup> As a result, the domination and control of a corporation is a prerequisite to piercing the veil.

The second part of the veil piercing test requires fraudulent activity or injustice that would be perpetrated by allowing a shareholder to enjoy limited liability.<sup>106</sup> The dominant view is that control of the corporation alone is not enough to pierce the corporate veil.<sup>107</sup> The existence of injustice is a loose standard, but most courts agree that merely the existence of an outstanding claim is not enough to satisfy this requirement.<sup>108</sup> Otherwise, any and all claims would pierce the corporate veil if successful on the

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<sup>100</sup> *Id.*

<sup>101</sup> *Id.*

<sup>102</sup> Empirical evidence demonstrates few, if any, publicly held corporations can be pierced. Thompson, *supra* note 2, at 1070.

<sup>103</sup> *Id.*

<sup>104</sup> Thompson, *supra* note 2, at 1063. When the term dummy is used, the rate of piercing increases to nearly ninety percent.

<sup>105</sup> Thompson, *supra* note 2, at 1064 n.141. Thompson notes that when the court notes domination of the corporation, the rate of pierce is less than sixty percent. When those factors are absent, it is almost universally fatal to the claim. Highlighting the absence of a single element leading to no piercing provides a more significant insight into the importance of that factor since it is singled out rather than mentioned in laundry list fashion.

<sup>106</sup> See, e.g., *Van Dorn Co. v. Future Chemical & Oil Corp.*, 753 F.2d 565, 570 (7th Cir. 1985); *Collet v. Am. Nat'l Stores, Inc.*, 708 S.W.2d 273, 284 (Mo. Ct. App. 1986).

<sup>107</sup> Satisfying the first prong alone is almost universally considered insufficient to pierce the veil. See *Shafford v. Otto Sales Co.*, 260 P.2d 269, 277 (Cal. Dist. Ct. App. 1953). But see *Walkovsky v. Carlton*, 223 N.E.2d 6, 6 (N.Y. 1966) (indicating that domination and control of a corporation is enough to establish the corporation is the shareholder's alter ego and therefore pierce the corporate veil).

<sup>108</sup> *Assoc. Venders, Inc. v. Oakland Meat Co.*, 26 Cal. Rptr. 806, 816 (Cal. Dist. Ct. App. 1962) (holding that it "is not sufficient to merely show that a creditor will remain unsatisfied if the corporate veil is not pierced.").

merits.<sup>109</sup> Most states require some form of active and intentional misconduct, not mere unfairness. The lack of guidance from the courts make ex/ante business organization planning difficult. Instead, courts often produce a list of factors influencing the decision to pierce the veil.<sup>110</sup> Some courts have indicated no less than twenty separate determinants influence veil piercing.<sup>111</sup> The most common criteria are fraud and misrepresentation.<sup>112</sup>

Fraud can include a variety of deceptive acts including anything from a fraudulent conveyance to forging documents to demonstrate the financial health of the firm.<sup>113</sup> Misrepresentation is a lower hurdle and can include misrepresenting corporate assets or the party responsible for payment.<sup>114</sup> Misrepresentation and fraud are the most important from a limited liability standpoint. Deceiving creditors about the corporation's capital formation hides critical facts from the cheapest cost avoider and prevents him or her from bargaining for personal security on the loan.<sup>115</sup> In other words, it allows the shareholder externalize the risk by shifting it to the creditor without the creditor's knowledge. The application of misrepresentation indicates that misrepresentation is considered a significant consideration in cases where the corporate veil is pierced.<sup>116</sup> The factor is cited most by courts and when it exists, the veil is pierced in over ninety-four percent of cases.<sup>117</sup> When the court notes the factor is absent, it goes on to pierce in only seven percent of cases.<sup>118</sup>

In sum, contractarian theory of limited liability indicates that attempts to pierce the veil should be most successful when there is a closely held firm and there is some misrepresentation or fraud involved. Despite the patchwork of case law about veil piercing, the majority of courts are

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<sup>109</sup> *Dombroski v. Wellpoint, Inc.*, 895 N.E.2d 538, 544-45 (Ohio 2008).

<sup>110</sup> In *Winger*, the court noted that many factors were relevant when considering a veil claim, including: "whether (1) the corporation is operated as a distinct business entity; (2) funds and assets are commingled; (3) adequate corporate records are maintained; (4) the nature and form of the entity's ownership and control facilitate misuse by an insider; (5) the business is thinly capitalized; (6) the corporation is used as a "mere shell"; (7) legal formalities are disregarded; and (8) corporate funds or assets are used for noncorporate purposes." *McCallum Family LLC v. Winger*, 221 P.3d 69, 74 (Colo. App. 2009).

<sup>111</sup> *Assoc. Venders, Inc.*, 26 Cal. Rptr. at 813-15.

<sup>112</sup> *Thompson*, *supra* note 2, at 1038.

<sup>113</sup> See *Torco Oil Co. v. Innovative Thermal Corp.*, 763 F. Supp 1445, 1451-52 (N.D. Ill. 1991) (for a discussion of facts in a veil piercing case leading to a finding of fraud).

<sup>114</sup> *Thompson*, *supra* note 2, at 1044 n.53.

<sup>115</sup> *Bainbridge*, *supra* note 13, at 503.

<sup>116</sup> *Thompson*, *supra* note 2, at 1066.

<sup>117</sup> *Id.* at 1063.

<sup>118</sup> *Id.* at 1065 n.142.

consistent: if a closely held firm is dominated by a single shareholder<sup>119</sup> who actively engages in fraud or misrepresentation of corporate assets or finances, the likelihood of piercing the corporation's veil is nearly a certainty. Despite commentary to the contrary, there is a solid core of activity that directly leads to veil piercing.<sup>120</sup>

### III. PIERCING THE CORPORATE VEIL IN OHIO: FROM *STANDARD OIL* TO *DOMBROSKI*

Like most states, Ohio has created an equitable remedy for misuse of the corporate form through corporate veil piercing.<sup>121</sup> In 1892, the Ohio Supreme Court first recognized the equitable remedy against the shareholders of a corporation in *State ex rel. Attorney General v. Standard Oil*.<sup>122</sup> In *Standard Oil*, the court noted that the corporate form was a fiction that bestowed on a group of individuals a legal identity. However, the corporate form may be disregarded when it is used "to an intent and purpose not within its reason and policy."<sup>123</sup>

The *Standard Oil* court reasoned that individuals could be acting either through their own legal identity or through the corporation.<sup>124</sup> It was the court's role to decide whether to attribute individual actions to the individual's legal identity or the corporation.<sup>125</sup> As a fiction of the law, the corporation cannot defeat the purpose for which it was invented.<sup>126</sup> Since a corporation could only be organized for a lawful purpose, actions by individuals that were unlawful could not be attributed to the corporation.<sup>127</sup> Any illegal actions were therefore the conduct of the shareholder and not the corporation. The alternative would permit shareholders to insulate themselves in the corporate form and provide practical personal immunity

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<sup>119</sup> Domination is shown by failing to observe formalities, mingling business and personal assets, failing to keep business records and thin capitalization. *McCallum Family LLC v. Winger*, 221 P.3d 69, 74 (Colo. App. 2009).

<sup>120</sup> That there is predictable activity leading to piercing is not to say there are never unpredictable decisions. *See, e.g., United States v. Toler*, 666 F. Supp. 2d 872, 886 (S.D. Ohio 2009) (noting incorrectly that control of the corporation was sufficient to pierce the corporate veil negating the need for *Belvedere's* second prong under Ohio law).

<sup>121</sup> *State ex rel. Attorney General v. Standard Oil Co.*, 30 N.E.2d 279, 287 (Ohio 1892).

<sup>122</sup> *Id.*

<sup>123</sup> *Id.* at 287.

<sup>124</sup> *Id.*

<sup>125</sup> *Id.*

<sup>126</sup> *Id.*

<sup>127</sup> *Id.* at 179.

for a host of offenses.<sup>128</sup> The *Standard Oil* court's analysis focused more on the concept of disregarding the corporate entity as opposed to piercing the corporate veil. The court recognized that it was the shareholder acting individually, not the corporation. Accordingly, it held the individual personally responsible, not the corporation.<sup>129</sup>

The *Standard Oil* court's articulated policy was not a practical test, ready for application in complex situations.<sup>130</sup> A few years later, in *First National Bank of Chicago v. F.C. Trebein Co.*, the Ohio Supreme Court held the two circumstances under which the corporate form would be disregarded: fraud and illegal activity.<sup>131</sup> Then in *North v. Higabee*, the Supreme Court flatly rejected the idea that unity of ownership was enough to pierce the corporate veil.<sup>132</sup> Instead the *North* court created a two-step test, requiring the party seeking to disregard the corporate entity to demonstrate first that "the corporation was formed to perpetrate a fraud and [second] the shareholder's control of the corporation was exercised to defraud the party."<sup>133</sup> The requirement that the corporation be *formed* to commit fraud was a high barrier to piercing any corporation's veil – even if that corporation had engaged in extensive illegal conduct.<sup>134</sup>

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<sup>128</sup> *Id.* at 287-88.

<sup>129</sup> The court's reasoning provided security for the corporate form. Theoretically, nothing could pierce the corporate veil since the corporation was organized for lawful purposes. Therefore, any unlawful activity of the corporation must be attributed to the individual, not the corporation. However practically, the court's disregard of the corporate form while providing the ultimate theoretical security, had the same effect as permitting the party to pierce the corporate veil.

<sup>130</sup> In *Standard Oil*, the court's syllabus held: "That a corporation is a legal entity, apart from natural person who compose it, is mere fiction . . . but like every other fiction of law, when urged to an intent and purpose not within its reason and policy, may be disregarded." *Id.* at 285. In Ohio, the syllabus has the weight of law. See *Akers v. Serv-A-Portion, Inc.*, 508 N.E.2d 964, 964 n.1 (Ohio 1987).

<sup>131</sup> *First Nat'l Bank of Chi. v. F.C. Trebein Co.*, 52 N.E.2d 834, 835 (Ohio 1898) (holding "A corporation cannot be formed for the purpose of accomplishing a fraud or other illegal act under the disguise of the fiction; and, when this is made to appear, the fiction will be disregarded by the courts."). However in *Trebein*, the court failed to directly mention one of the primary modern requirements of most veil-piercing tests: unity of interest and ownership. See *Sea-Land Services, Inc. v. Pepper Source*, 941 F.2d 519, 520 (7th Cir. 1991). But, its application notes that the corporation is usually owned almost entirely by one individual. *Trebein*, 52 N.E.2d at 838.

<sup>132</sup> *North v. Higbee*, 3 N.E.2d 391, 395 (Ohio 1936).

<sup>133</sup> *Id.* at 391.

<sup>134</sup> *Belvedere*, 617 N.E.2d at 1086 (noting "it seems that in practice it would be unreasonably difficult to prove that any corporate on was actually *formed* in order to perpetrate a fraud."). Under the *North* rule, even the most egregious acts could insulate the individual if the corporation was formed for a legitimate purpose. The ease of forming corporations under state law and the ability to transfer ownership

Finally, in 1993, the Ohio Supreme Court created the modern test in *Belvedere Condominium Unit Owners’ Association. v. R.E. Roark Cos., Inc.*<sup>135</sup> The court held there was a three pronged inquiry: (1) whether the corporation was the alter ego of the individual which would render the individual and corporation fundamentally indistinguishable, (2) whether control was exercised to commit fraud or an illegal act and (3) an injury or loss resulted to the plaintiff from such control and wrong.<sup>136</sup>

#### A. Pre-Dombroski: *The Difference of Opinion*

Prior to *Dombroski* in 2007, Ohio appellate courts had set up two distinct camps interpreting *Belvedere*.<sup>137</sup> The majority of courts recognized that *Belvedere*’s second prong, requiring “fraud or illegal activity,” was not explicitly limited to those circumstances.<sup>138</sup> Other considerations such as “harm, injustice, or fundamental unfairness” could satisfy the second *Belvedere* element.<sup>139</sup> The Third, Seventh, Tenth, Eleventh, and Twelfth District Courts of Appeals adopted the more expansive view.<sup>140</sup> Even the federal Sixth Circuit Court of Appeals adopted the more liberal

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meant a corporation could be formed for a perfectly legitimate and legal purpose only to later be an instrument of fraud. *North*, 3 N.E.2d at 391.

<sup>135</sup> *Belvedere*, 617 N.E.2d at 1075.

<sup>136</sup> *Id.* at 289.

<sup>137</sup> See *Wiencek v. Atcole Company, Inc.*, 671 N.E.2d 1339, 1342 (Ohio App. 3d Dist. 1996). But see *Collum v. Perlman*, No. L-98-1291, 1999 WL 252725, at \*3 (Ohio App. 6th Dist. Apr. 30, 1999).

<sup>138</sup> *Id.*

<sup>139</sup> *Wiencek*, 671 N.E.2d at 1342.

<sup>140</sup> 26-11 FLETCHER CORP. LAW ADVISOR art. VII (2008). See, e.g., *Robert A. Saurber Gen. Contr., Inc. v. McAndrews*, CA2003-09-239, 2004 WL 2937627, at \*5 (Ohio App. 12th Dist. Dec. 20, 2004); *State v. Tri-State Group, Inc.*, No. 03BE61, 2004 WL 1882567, at \*14 (Ohio App. 7th Dist. Aug. 20, 2004); *Sanderson Farms, Inc. v. Gasbarro*, No. 01AP-461, 2004 WL 583849, at \*8 (Ohio App. 10th Dist. Mar. 25, 2004); *Stypula v. Chandler*, No. 2002-G-2468, 2003 WL 22844296, at \*3 (Ohio App. 11th Dist. Nov. 26, 2003); *Dalicandro v. Morrison Road Dev. Co., Inc.*, No. 00AP-619, 2001 WL 379893, at \*7 (Ohio App. 10th Dist. Apr. 17, 2001); *Pritchett, Dlusky & Saxe v. Pingue*, 96APE11-1598, 1997 WL 578952 (Ohio App. 10th Dist. Sept. 16, 1997); *Wiencek*, 671 N.E.2d at 1342 (“Based upon a reading of *Belvedere*, the purpose of the ‘piercing the corporate veil’ theory, and Ohio case law prior to and subsequent to *Belvedere*, we hold that one seeking to disregard the corporate entity may present evidence that the shareholder exercised his control over the corporation in such a manner as to commit a fraud, illegal, or other unjust or inequitable act upon the person seeking to disregard the corporate entity in order to satisfy the second prong of the test enunciated in *Belvedere*.”).

interpretation.<sup>141</sup> However, the Sixth District Court of Appeals in *Collum v. Perlman* concluded that 'fraud or illegal act' was literally limited to fraud or illegal conduct.<sup>142</sup> Absence of one of the factors was fatal to any veil piercing claim, regardless of the equity or fairness.<sup>143</sup>

In fact, because of the ambiguous foundation of *Belvedere's* second prong both positions were well reasoned. The courts favoring a liberal interpretation noted that prior to *Belvedere*, the Ohio Supreme Court had seemed to indicate that "the perpetuation of a fraud or illegality is not the sole ground for disregarding the corporate entity."<sup>144</sup> In *Auglaize Box Board Co. v. Hinton*, the Ohio Supreme Court held in addition to fraud or illegality, the corporate form "should be disregarded only when justice cannot be served in any other way."<sup>145</sup> Similarly in *Thrift Fed. S.&L. Assn. v. Overton*, the Ohio Supreme Court noted that the corporate entity could be disregarded since the "individualities of the [person] and this corporation are nonexistent."<sup>146</sup> The ambiguity of the court's language in *Overton*, resulted in two possible interpretations: either only unity of ownership was necessary for the corporation's veil to be pierced or the corporate veil could be pierced in situations where fraud and illegality were not present.<sup>147</sup> The appellate courts picked up on this language and expanded the equitable doctrine to situations beyond fraud or other illegality.

The Ohio Supreme Court's decision in *Belvedere* did nothing to clear the rapidly muddying waters. While the decision laid out a practical three-pronged test for corporate veil piercing, it did not address the mounting confusion in the lower courts. In fact, the court complicated the situation by adopting a test that was not exclusively limited to fraud or illegal acts. In *Belvedere*, the corporate veil piercing test Ohio adopted was taken from the Sixth Circuit's decision in *Bucyrus-Erie Co. v. General Products Corp.*<sup>148</sup> The second prong of the Sixth Circuit's veil piercing test included both fraud and illegality, but also included "other dishonest or unjust acts . . . ."<sup>149</sup> The *Belvedere* court quoted *Bucyrus* favorably

<sup>141</sup> *Taylor Steel, Inc. v. Keeton*, 417 F.3d 598, 609 (6th Cir. 2005) (noting "Ohio courts have recognized that although the *Belvedere* court used 'fraud' and 'criminal activity' in defining the second prong, the true question to be asked is whether it would be unjust under the circumstances of each case . . . .").

<sup>142</sup> *Collum*, 1999 WL 252725, at \*3.

<sup>143</sup> *Id.*

<sup>144</sup> *LeRoux's Billyle Supper Club v. Ma*, 602 N.E.2d 685, 688 (Ohio App. 6th Dist. 1991) (citing *E.S. Preston Assoc., Inc. v. Preston*, 92 N.E.2d 441, 446 (Ohio 1986)).

<sup>145</sup> *E.S. Preston Assoc.*, 92 N.E.2d at 446.

<sup>146</sup> *Thrift Fed. S.&L. Ass'n v. Overton*, 563 N.E.2d 289, 293 (Ohio 1990).

<sup>147</sup> *Id.*

<sup>148</sup> *Belvedere Condominium Unit Owners' Ass'n. v. R.E. Roark Cos., Inc.*, 617 N.E.2d 1075, 1086 (Ohio 1993).

<sup>149</sup> *Bucyrus-Erie Co. v. Gen. Products Corp.*, 643 F.2d 413, 418 (6th Cir. 1981).

indicating that the holding “strikes the correct balance between the principle of limited shareholder liability and the reality that the corporate fiction is sometimes used by shareholders to protect themselves from liability for their own misdeeds.”<sup>150</sup> However, when the Ohio Supreme Court restated its own test in *Belvedere*, it cut the language from *Bucyrus* that included inequitable or unfair actions, other than fraud or illegality.<sup>151</sup>

The Ohio Supreme Court’s removal of ‘other dishonest or unjust acts’ in a test that otherwise reproduces the Sixth Circuit’s holding is a glaring – and seemingly intentional – omission.<sup>152</sup> However, the earlier reliance on an expansive reading of veil piercing likely made the district appellate court judges hesitant to overrule their own clear precedent without an affirmative indication from the Ohio Supreme Court. Since the divergent views in the districts already existed prior to *Belvedere* and the Ohio Supreme Court did not take any steps in *Belvedere* to clarify, the district courts held to their precedent allowing unjust or inequitable acts to pierce the corporate veil.<sup>153</sup> The lower courts in Ohio were faced with a decision: conclude that the omission of unjust act from *Belvedere* was an oversight (since the Ohio Supreme Court favorably cited a case which included it) or conclude the omission was purposeful despite no indication the court was overruling other precedent. In *Dombroski v. WellPoint Inc.*, the Ohio Supreme Court attempted to clarify the confusion of whether the second

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<sup>150</sup> *Belvedere*, 617 N.E.2d at 1086.

<sup>151</sup> *Id.* (holding “control over the corporation by those to be held liable was exercised in such a manner as to commit fraud or an illegal act against the person seeking to disregard the corporate entity . . .”).

<sup>152</sup> Compare *Belvedere*, 617 N.E.2d 1075 at 1086 (holding the corporate entity may be disregarded when “(1) control over the corporation by those to be held liable was so complete that the corporation has no separate mind, will, or existence of its own, (2) control over the corporation by those to be held liable was exercised in such a manner as to commit fraud or an illegal act against the person seeking to disregard the corporate entity, and (3) injury or unjust loss resulted to the plaintiff from such control and wrong.”) with *Bucyrus*, 643 F.3d at 418 (holding the corporate entity may be disregarded when “(1) domination and control over the corporation by those to be held liable is so complete that the corporation has no separate mind, will, or existence of its own; (2) that domination and control was used to commit fraud or wrong or other dishonest or unjust act, and (3) injury or unjust loss resulted to the plaintiff from such control and wrong.”).

<sup>153</sup> Furthermore, the federal courts persist in holding that the first step of the *Belvedere* test is itself a basis for disregarding limited liability. See *In re Fisher*, No. 07-3319, 2008 WL 4569946, at \*5 (6th Cir. Oct. 10, 2008); *Toler*, 666 F. Supp. 2d at 886. In other words, there is an erroneous belief that control and domination alone are sufficient to pierce the corporate veil. *Dombroski v. Wellpoint, Inc.*, 895 N.E.2d 538, 545 (Ohio 2008) (“The first and third prongs of the *Belvedere* . . . must still be met for a piercing claim to succeed.”).

*Belvedere* prong could allow conduct less than fraud or illegality to pierce the veil.<sup>154</sup>

*B. Fraud or Inequity: Is there any Difference?*

The difference between allowing mere inequity or unfairness to satisfy the requirement for veil piercing and requiring fraud or illegal conduct is a broad one, at least theoretically. The fraud or illegality requirement erected by the Sixth District in *Collum* posed a much stricter barrier to parties attempting to pierce the corporate veil. For example in *Collum*, financial problems forced the defendant Perlman to close his corporate enterprise, Wholesale Lighting.<sup>155</sup> After liquidating the company's assets, Perlman paid off sales taxes in Michigan and Ohio in addition to payroll taxes.<sup>156</sup> Left outstanding was nearly \$50,000 in unpaid debts, including over \$9,000 to Collum.<sup>157</sup> The Sixth District concluded that there was no fraud or illegal action taken by Perlman – only an inability to pay outstanding debts.<sup>158</sup> As a result, the second prong of *Belvedere* was not satisfied and the court reversed the trial court's award to Collum.<sup>159</sup> Similarly in *Widlar v. Young*, the Sixth District held that a mere breach of contract could not amount to fraud or illegal conduct which would justify piercing the corporate veil.<sup>160</sup>

In contrast, the majority of districts permitted a wide range of activities to justify the second prong of *Belvedere* when it was interpreted to include inequity or unfairness.<sup>161</sup> In *Stypula v. Chandler*, the Eleventh

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<sup>154</sup> *Dombroski*, 895 N.W.2d at 539.

<sup>155</sup> *Collum v. Perlman*, No. L-98-1291, 1999 WL 252725, at \*2 (Ohio App. 6th Dist. Apr. 30, 1999).

<sup>156</sup> *Id.*

<sup>157</sup> *Id.*

<sup>158</sup> *Id.* at \*3.

<sup>159</sup> *Id.* at \*4.

<sup>160</sup> *Widlar v. Young*, No. L-05-1184, 2006 WL 456724, at \*6 (Ohio App. 6th Dist. Feb. 24, 2006).

<sup>161</sup> While these courts permitted a broad reading of *Belvedere*, in reality, the liberal reading was often unnecessary. In *Young* and *Stypula*, the existence of fraud by the defendants was plain. The courts held that the defendants committed fraud or the facts made fraud fairly apparent. *Young*, 2006 WL 456724, at \*6; *Stypula v. Chandler*, No. 2002-G-2468, 2003 WL 22844296, at \*3 (Ohio App. 11th Dist. Nov. 26, 2003). In *Stypula*, the defendant transferred assets from one corporation to another, with the specific intent to avoid paying a creditor. *Stypula*, 2003 WL 22844296, at \*3. In *Young*, the court held that the defendant committed fraud. *Young*, 2006 WL 456724, at \*6. Also in *Sanderson Farms, Inc. v. Gasbarro*, the defendant asset transfers were fraudulent since the defendant had constructive intent to defraud creditors and the transfers left the corporation totally insolvent. *Sanderson Farms, Inc.*, 2004 WL 583849, at \*12. However, in each of these cases, the appellate court concluded inequitable circumstances could justify piercing the corporate veil.



District permitted a plaintiff to pierce the corporation’s veil because the defendant closed the corporation after a judgment was entered against the corporation.<sup>162</sup> Then the defendant created a new corporation, rehired all the same employees and operated the same business with the same clients out of the same office three days later.<sup>163</sup> The court concluded that permitting the corporate form to shield the defendant in such a situation was inequitable and allowed the plaintiff to pierce the corporation’s veil.<sup>164</sup> Similarly, in *Wiencek v. Atcole Co.*, the Third District permitted the plaintiff to pierce the defendant’s corporate veil since the shareholders gave themselves large bonuses as officers of the corporation and used corporate assets for personal purchases.<sup>165</sup> The court concluded these actions may have depleted profits to an extent that prevented payment to a creditor.<sup>166</sup> The Court of Appeals for the Twelfth District agreed with the *Weincek* court’s reasoning to permit unjust circumstances to suffice for piercing the corporate veil.<sup>167</sup>

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<sup>162</sup> *Stypula*, 2003 WL 22844296, at \*3.

<sup>163</sup> *Id.*

<sup>164</sup> The court’s expansive reading for the second *Belvedere* prong was entirely unnecessary in this context. Instead, what the defendant did was plainly a fraudulent transfer which fulfilled the second prong of *Belvedere* even under its literal reading. The defendant fraudulently transferred assets since the transfer occurred after the debt was incurred and was done with the intent to defraud. *Id.* See OHIO REV. CODE ANN. § 1336.04(A) (West 2009) (Ohio’s Fraudulent Transfer Act); see also OHIO REV. CODE ANN. § 1336.04(B) (factors to consider in finding a fraudulent transfer).

<sup>165</sup> *Wiencek*, 671 N.E.2d at 1343 (noting that the defendants “gave themselves very large bonuses as officers of the corporation, used Atcole to pay for [both] labor (by an Atcole employee) and material that the [defendant]’s personal residence, and purchased a recreational vehicle in the corporate name which was used by the [defendants], but not for corporate purposes.”).

<sup>166</sup> *Id.* at 1343.

<sup>167</sup> *Robert A. Saurber Gen. Contr., Inc. v. McAndrews*, CA2003-09-239, 2004 WL 2937627, at \*5 (Ohio App. 12th Dist. Dec. 20, 2004). However, the court’s expansive reading of the second prong of *Belvedere* was unnecessary since the court also noted that the defendant defrauded the plaintiff by submitting affidavits claiming reimbursements for claims which other suppliers held. When the defendant received a joint check for the amount, he cashed the checks without the signatures of the other suppliers and failed to reimburse them. The court noted the existence of fraud, but expanded *Belvedere*’s second element anyway. *Id.* at 5-6.

C. Dombroski: *Potato or Potahto, Illegal or Unlawful*<sup>168</sup>

*Dombroski* was the Ohio Supreme Court's opportunity to set the record straight on veil piercing in Ohio. The facts of *Dombroski* were straightforward. The plaintiff was Kimberly Dombroski, who was insured by Community Insurance Company (CIC).<sup>169</sup> In 2000, Dombroski received a cochlear implant in her left ear.<sup>170</sup> By 2005, her doctor determined that a similar implant was necessary for her right ear.<sup>171</sup> However, CIC denied coverage for the procedure by concluding that the implant was investigational.<sup>172</sup> Dombroski appealed the decision through the company's internal process, but was unsuccessful.<sup>173</sup>

Dombroski filed suit against CIC in 2006 alleging insurer bad faith, breach of insurance contract, and promissory estoppel.<sup>174</sup> The case originated in the Seventh District, which had accepted the expansive reading of the second prong of *Belvedere* that included unjust or inequitable acts.<sup>175</sup> Dombroski also named WellPoint, Inc. as a defendant in the suit since CIC was a subsidiary of WellPoint.<sup>176</sup> WellPoint was not a party to the insurance contract.<sup>177</sup> However, Dombroski claimed that WellPoint was liable for the actions of its subsidiary since she could pierce CIC's corporate veil.<sup>178</sup> The complaint alleged that CIC was wholly controlled by WellPoint.<sup>179</sup> CIC's stock was entirely controlled by WellPoint, WellPoint and CIC had the same officers and directors, and WellPoint controlled CIC to such a degree that CIC had no independent existence.<sup>180</sup> Dombroski also claimed that this subsidiary-parent relationship existed "to violate the duty of good faith and fair dealings to its Ohio insureds, specifically Dombroski."<sup>181</sup> The trial court concluded Dombroski failed to state a claim and dismissed the complaint.<sup>182</sup>

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<sup>168</sup> *Dombroski v. Wellpoint, Inc.*, 895 N.E.2d 538, 545-46 (Ohio 2008) (Pfeifer, J., dissenting).

<sup>169</sup> *Dombroski*, 879 N.E.2d at 228.

<sup>170</sup> *Id.*

<sup>171</sup> *Id.*

<sup>172</sup> *Id.*

<sup>173</sup> *Dombroski*, 895 N.E.2d at 541.

<sup>174</sup> *Dombroski*, 879 N.E.2d at 228.

<sup>175</sup> *State v. Tri-State Group, Inc.*, No. 03BE61, 2004 WL 1882567, at \*14 (Ohio App. 7th Dist. Aug. 20, 2004).

<sup>176</sup> *Id.*

<sup>177</sup> *Id.* at 229.

<sup>178</sup> *Id.*

<sup>179</sup> *Dombroski*, 879 N.E.2d at 228.

<sup>180</sup> *Id.*

<sup>181</sup> *Id.* at 228.

<sup>182</sup> *Id.* at 229.

On appeal to the Seventh District, the court reversed the decision of the trial court by holding Dombroski had stated a claim to relief against WellPoint through corporate veil piercing.<sup>183</sup> The court noted the substantial precedent interpreting the second prong of *Belvedere* to include unjust or inequitable acts.<sup>184</sup> The trial court had interpreted Dombroski's claim as a simple breach of contract that did not rise to the level of unjust or inequitable acts.<sup>185</sup> However, the Seventh District noted that in the insurance context, even a simple breach of contract claim involved a question of the duty of good faith.<sup>186</sup> In Ohio, the relationship between the insurer and insured requires the insurer to "act in good faith in the handling and payment of the claims of its insured."<sup>187</sup> The court concluded that any breach of the insurer's duty of good faith is an unjust or inequitable act that may form the basis of a claim of corporate veil piercing.<sup>188</sup> The second prong of *Belvedere* was therefore apparent on the pleadings and the trial court had dismissed the complaint in error.<sup>189</sup> The court of appeals determined that its decision was in direct conflict with the judgment of the Sixth District Court of Appeals and certified the case as a conflict to the Ohio Supreme Court.<sup>190</sup> The Ohio Supreme Court took the case to resolve the split in Ohio's districts.<sup>191</sup>

The Ohio Supreme Court rejected the broad reading of *Belvedere*'s second prong and held that parties seeking to pierce the corporate veil must allege the literal language of *Belvedere*: fraud or illegal act.<sup>192</sup> The court reasoned that piercing the corporate veil is a "rare exception to be applied only in the case of fraud or certain other exceptional circumstances."<sup>193</sup> While a shareholder is never totally immune for the actions of their corporation, only criminal conduct or fraud to the detriment of a third party gives rise to liability.<sup>194</sup> This ensures that the corporation and the individual

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<sup>183</sup> *Id.* at 231.

<sup>184</sup> *Dombroski*, 879 N.E.2d at 231.

<sup>185</sup> *Id.*

<sup>186</sup> *Id.* at 232 (citing *Hoskins v. Aetna Life Ins. Co.*, 452 N.E.2d 1315, 1315 (Ohio 1983)).

<sup>187</sup> *Dombroski*, 879 N.E.2d at 232.

<sup>188</sup> *Id.* at 233.

<sup>189</sup> *Id.*

<sup>190</sup> *Dombroski*, 895 N.E.2d at 541-42.

<sup>191</sup> *Dombroski* came before the Ohio Supreme Court through a certified conflict under Section 3(b)(4), Art. IV, Ohio Constitution and Ohio Appellate Rule 25. See OHIO CONST. ART. IV, § 3(B)(4); OHIO APP. R. 25 (West 2009).

<sup>192</sup> *Dombroski*, 895 N.E.2d at 544.

<sup>193</sup> *Id.* at 542-43 (citing *Dole Food Co. v. Patrickson*, 538 U.S. 468, 475 (2003) (internal quotations removed)).

<sup>194</sup> *Id.*

remain separate entities and prevents corporate veil piercing every time a closely held corporation is sued.<sup>195</sup> The court noted the literal language of *Belvedere*'s second prong ensured the correct balance between limited shareholder liability and misuse of the corporate form.<sup>196</sup> As a result, the court concluded that unjust or inequitable conduct "is simply too broad to survive exacting review" and severed *Belvedere*'s reliance on *Bucyrus*.<sup>197</sup>

The court could have stopped writing and completed its review by clearly explaining the limits of corporate veil piercing. However, the court observed that *Belvedere* rule was too limited to "protect other potential parties from the wide variety of egregious shareholder misdeeds that may occur."<sup>198</sup> Under the literal language of *Belvedere*, shareholders could misuse the corporate form and evade liability when the shareholders "abuse the corporate form to commit acts that are *as objectionable as fraud or illegality*."<sup>199</sup> To pierce the corporate veil, the court concluded plaintiffs must demonstrate fraud, illegality, or a "similarly unlawful act," but cautioned courts to avoid applying the new test expansively.<sup>200</sup>

The court's new rule has created problems. Currently, the outer boundaries of the new doctrine of veil piercing are unknown. The Ohio Supreme Court, in deciding between *Belvedere* options *A* or *B*, created a third choice, *C*, which was neither derived from case law nor explained by the court. The Ohio Supreme Court's only guidance for practitioners and entrepreneurs interpreting its decision was that its new rule was somewhere between the liberal 'unfairness or inequity' rule and 'fraud or illegality.' But where on the spectrum did it fall? Closer to inequity or illegality? The court seemed to suggest the latter, but the vagueness of the opinion leaves the question up in the air.

Justice Pfeifer's dissent attacks the majority on this issue – pointing out that the additional language "[i]nstead of resolving the conflict . . . has muddied the waters."<sup>201</sup> Pfeifer notes: "[t]he new language seems to be

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<sup>195</sup> *Id.* at 544-45 (noting if the court "[w]ere [] to allow piercing every time a corporation under the complete control of a shareholder committed an unjust or inequitable act, virtually every close corporation could be pierced when sued, as nearly every lawsuit sets forth a form of unjust or inequitable action and close corporations are by definition controlled by an individual or small group of shareholders.").

<sup>196</sup> *Dombroski*, 895 N.E.2d at 544-45.

<sup>197</sup> *Id.* at 545. The court also ignored the insurer bad faith issue. Since the case had reached the Ohio Supreme Court on a certified conflict, the court did not address the question. *Id.* at 512 n.2.

<sup>198</sup> *Id.*

<sup>199</sup> *Id.* (emphasis added).

<sup>200</sup> *Id.* ("Courts should apply this limited expansion cautiously toward the goal of piercing the corporate veil only in instances of extreme shareholder misconduct.").

<sup>201</sup> *Dombroski*, 895 N.E.2d at 546 (Pfeifer, J., dissenting).

pulled from the air. Is there a notable distinction between an "unlawful" and an "illegal" act? Not that the majority identifies. The words appear to be two ways of saying the same thing. Potato, potahto, illegal, unlawful – let's call the whole thing off."<sup>202</sup>

#### IV. THE AFTERMATH: IS OHIO BETTER OFF POST-*DOMBROSKI*?

The short answer is corporate law in Ohio benefitted from *Dombroski*. However, the benefit is qualified. Since *Dombroski*, there has not been a significant judicial discussion of the addition of the phrase "similarly unlawful act" to the second step of the *Belvedere* test.<sup>203</sup> Most cases have easily fallen into the pre-*Dombroski* categories of fraudulent/illegal or simply amounting to unjust actions that cannot lead to veil piercing.<sup>204</sup> No court has been willing to draw a line between inequality and fraudulent/illegal conduct to define the outer boundaries of veil piercing in Ohio.<sup>205</sup> Despite the lack of judicial response, the *Dombroski* court indicated the direction corporate law is heading in Ohio enough to permit meaningful speculation regarding the court's goals. Examining the policy of limited liability in conjunction with the court's new language indicates the *Dombroski* rule is a standard that permits piercing when conduct is in the ambit of fraudulent or illegal activity.

Consider the structure of conduct the Ohio Supreme Court created for veil piercing cases. On a hypothetical spectrum, on one extreme is fraud or illegal conduct and at the other is simple unfairness. Allowing judges nearly boundless discretion to pierce the veil when there is unfairness is a fairly liberal piercing policy.<sup>206</sup> If the Ohio Supreme Court permitted mere

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<sup>202</sup> *Id.* at 547 (Pfiefer, J., dissenting).

<sup>203</sup> *Id.* at 545.

<sup>204</sup> Compare *Transition Healthcare Assoc., Inc. v. Tri-State Health Investors, LLC*, 306 Fed. Appx 273, 282 n.14 (6th Cir. 2009) (denying veil piercing claim under *Dombroski*) with *Advantage Bank v. Waldo Pub LLC*, No. 9-08-67, 2009 WL 1664781 (Ohio App. 3d Dist. June 15, 2009) (denying veil piercing under previous *Belvedere* standard).

<sup>205</sup> Some conduct, such as a simple contract breach, falls beyond the second *Belvedere* prong. See *Connolly v. Malkamaki*, No. 2001-L-124, 2002 WL 31813040, at \*6 (Ohio App. 11th Dist. Dec. 13, 2002). Other actions which are similar to fraud or illegal conduct fall within the test.

<sup>206</sup> One unspoken goal of the Ohio Supreme Court may have been to drastically limit the piercing rate in Ohio. Professor Thompson's statistical break down of veil piercing cases indicates that while the total number of cases seeking veil piercing is not huge compared to other states, Ohio ranks near the top for successful veil piercing. Thompson, *supra* note 2, at 1051. Close to sixty percent of claims seeking veil piercing as a remedy are successful in Ohio. *Id.* (noting a 57.14% success rate). The majority in *Dombroski* may have simply wanted to bring Ohio

unfairness to satisfy the test, the result would be every corporation's veil would be pierced in almost every situation.<sup>207</sup> In *Dombroski*, the Ohio Supreme Court nixed one end of the spectrum concluding that simple unfairness forced Ohio corporations and shareholders to internalize far too much risk.<sup>208</sup> At the same time, limiting veil piercing to cases of fraud or illegal activity "insulates shareholders when they abuse the corporate form to commit acts that are as objectionable as fraud or illegality."<sup>209</sup> The court concluded the conduct test needed to be realigned and inserted a third point into the conduct spectrum: similar unlawful acts.<sup>210</sup>

The court indicated that this new third point on the spectrum falls remarkably close to the conduct already described. First, the standard covers only "egregious wrongs" committed by shareholders.<sup>211</sup> Second, the court emphasized its point by urging caution in applying its new test.<sup>212</sup> The court's language is indefinite, but indicates that its goal is to prevent serious misuse of the corporate form without any specific examples of the activity it is concerned with deterring.<sup>213</sup> The Ohio Supreme Court's other recent veil piercing case supports the trend of stringently limiting the applicability of veil piercing. In *Minno v. Pro-Fab, Inc.*, the Ohio Supreme Court held parties could not use the doctrine of veil piercing to hold a second corporation liable for the debts of a sister corporation.<sup>214</sup> In other words, a party could not reverse veil pierce by using a common shareholder of two corporations as a conduit between the corporation being sued and the corporation having the capital to satisfy the judgment.<sup>215</sup> While the ability to reverse pierce had never been recognized by the Ohio Supreme Court prior to *Minno*, the case represents the court's enthusiasm for providing more security for limited liability. But the question remains what does the new language specifically add to *Belvedere*?

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into line with most other states. The national average rate for successful state court piercing is just under forty percent. *Id.* at 1049.

<sup>207</sup> *Dombroski v. Wellpoint, Inc.*, 895 N.E.2d 538, 546 (Ohio 2008).

<sup>208</sup> *Id.* at 544.

<sup>209</sup> *Id.* at 545.

<sup>210</sup> *Id.*

<sup>211</sup> *Id.*

<sup>212</sup> *Dombroski*, 895 N.E.2d at 545 ("Courts should apply this limited expansion cautiously toward the goal of piercing the corporate veil only in instances of extreme shareholder misconduct.").

<sup>213</sup> *Dombroski*, 895 N.E.2d at 544 (noting that piercing should be applied "only in case of . . . exceptional circumstances").

<sup>214</sup> *Minno v. Pro-Fab, Inc.*, 905 N.E.2d 613, 617 (Ohio 2009).

<sup>215</sup> *Id.* (The Court declined to permit reverse piercing because a "wrongful act committed by one sister corporation might have been instigated by the corporation's owners, but it could not have been instigated by the corporation's sister.").

The easy answer is misrepresentation because it is conduct that is the closest to fraud or illegality. The contractarian theory indicates that only under certain circumstances should there be an exception to limited liability: specifically when there is misrepresentation or fraud by the shareholder.<sup>216</sup> The *Belvedere* test explicitly includes fraud. The additional language from *Dombroski* may have been added to include actions such as misrepresentation. Though fraud and misrepresentation are similar, misrepresentation is a lesser standard.<sup>217</sup> In most states, common law fraud is a difficult standard to prove. In Ohio, there are six essential elements to proving fraud: representation or concealment of a fact, materiality, knowledge or recklessness with regard to its falseness, intent to mislead, justifiable reliance, and injury.<sup>218</sup> Misrepresenting a fact is only one part to the specific offense of fraud. Since misrepresentation is only an element of fraud, it generally covers much broader conduct.<sup>219</sup>

The distinction between the two standards results from the scienter requirement. Misrepresentation may only require confusion, as opposed to a positive misstatement.<sup>220</sup> For example in *My Bread Baking Co. v. Cumberland Farms, Inc.*, the court held the corporation's veil could be

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<sup>216</sup> Bainbridge, *supra* note 13, at 503.

<sup>217</sup> Thompson, *supra* note 2, at 1075 n.53. The standards must have some significant difference. If the plaintiff had a viable fraud case, he or she would plead it. *Id.* However, since fraud evidence is difficult to find, most parties attempting to pierce the corporate veil settle for misrepresentation. Cathy S. Krendl & James R. Krendl, *Piercing the Corporate Veil, Focusing the Inquiry*, 55 DEN. L.J. 1, 31 (1978) (noting that "fraud is difficult to prove, and the quantum of evidence available in most corporate veil cases is considerably smaller than would be required to carry the burden in a fraud claim.").

<sup>218</sup> *Tokles & Son, Inc. v. Midwestern Indemn. Co.*, 605 N.E.2d 936, 944 (Ohio 1992), *overruled on other grounds recognized by* *Morland v. Allstate Ins. Co.*, No. 266, 2000 WL 184600 (Ohio App. 7th Dist. Feb. 3, 2000). There is an indication from some Ohio courts that the scienter element of fraud can be satisfied if the party making the representation should have known of its falseness. *See Fenstermaker v. Elwood*, 479 N.E.2d 908, 913 (Ohio App. 3d Dist. 1984).

<sup>219</sup> The Second Restatement of Torts makes a similar distinction. A fraudulent misrepresentation occurs when the maker "knows or believes that the matter is not as he represents it to be [or] does not have confidence in the accuracy of his representation." All fraud is misrepresentation, but not all misrepresentation is fraud. RESTATEMENT (SECOND) OF TORTS § 526 (2009).

<sup>220</sup> *Krendl & Krendl, supra* note 217, at 32-33. For example, in *My Bread Baking Co. v. Cumberland Farms, Inc.*, the court held the corporation's veil court be pierced when the plaintiff only showed that the defendant ran several corporations from the same location and used common names. *My Bread Baking Co. v. Cumberland Farms, Inc.*, 233 N.E.2d 748, 753 (Mass. 1968). *See also* *Zaist v. Olson*, 227 A.2d 552, 552 (Conn. 1967).

pierced when the plaintiff only showed that the defendant ran several corporations from the same location and used common names.<sup>221</sup> The defendant was the dominant shareholder in a parent corporation that had several incorporated subsidiaries.<sup>222</sup> The defendant issued statements from his primary corporation on behalf of each subsidiary to the plaintiff who wished to distribute baking goods to the corporation.<sup>223</sup> Based on the defendant's communication, the plaintiff believed he was contracting with the primary corporation for distribution, not the subsidiaries.<sup>224</sup> The defendant did not indicate on which corporation's behalf he was acting when the communications were sent.<sup>225</sup> The court indicated that the "serious ambiguity" resulting from the situation, justified disregarding the corporate entity.<sup>226</sup> As a result, misrepresentation could pierce the veil, though it fell short of what would commonly be classified as fraud. The addition to *Belvedere's* conduct element is formulated to include misrepresentation – actions which are not themselves fraudulent, but similar in their nature and impact.<sup>227</sup>

The addition of misrepresentation to the test still leaves unresolved issues. After all, if the *Dombroski* court had only meant to include misrepresentation in its analysis, it would have explicitly added it. Instead, the court seemed determined that the law would retain some uncertainty. The lack of specific examples may provide one simple explanation for the court's additional language: additional discretion to judges. While the court could have simply listed the variety of acts which will satisfy the conduct element, doing so would bind judges from creating the most just remedy. The uncertainty of veil piercing has significant roots in its equitable foundation – judges ultimately see that justice is done to the litigating parties before considering *ex ante* issues. While *Dombroski* seriously limited the discretion of judges in veil piercing cases, the justices' addition of "similar unlawful acts" might indicate a reservation of judgment for

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<sup>221</sup> *My Bread Baking Co.*, 233 N.E.2d at 753.

<sup>222</sup> *Id.*

<sup>223</sup> *Id.* In this case, it seems entirely reasonable that the plaintiff would have been confused by the actions of the defendant. The defendant's actions lead the plaintiff to believe he was dealing with the parent corporation when in reality he was forming a series of agreements with each subsidiary.

<sup>224</sup> *Id.*

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* at 752. While the court seemed to indicate the lack of formalities between corporations was the issue, failure to keep entities distinct was not the problem. Instead, it exemplified the corporation's misrepresentation to its creditor that the creditor was dealing with the primary corporation, not its retail subsidiaries.

<sup>227</sup> This lesser standard makes veil piercing available in cases where the parties seeking to pierce the veil is unsophisticated or unable to bear the expenses of conducting a detailed financial audit of the corporation. Krendl & Krendl, *supra* note 217, at 33-34.



situations that have yet to be anticipated. In other words, the court retained an ace in the hole, the ability to decide unforeseen cases in a matter which the justices believe is most representative of fairness, but may fall outside of the strict legal framework of the *Belvedere* test.<sup>228</sup>

*Dombroski* both helped and hurt corporate law in Ohio. The Ohio Supreme Court in cases like *Dombroski* and *Minno* seemed determined to bring Ohio more into line with the attitudes of other states when it comes to limited liability. But, the court was also determined to keep equity somewhere in the equation. While this approach has the advantage of providing flexibility to judges in veil piercing cases, it creates the same hindrance that plagues veil piercing in every context: a lack of predictability. To the businessman, predictability is key to successful private ordering.<sup>229</sup> While the *Dombroski* decision may have satisfied the Ohio Supreme Court, it leaves some concrete issues unresolved for Ohio's corporations.

## V. CONCLUSION

Ohio is home to over 90,000 incorporated business entities.<sup>230</sup> Of these, sixty-one percent are operated by a sole shareholder.<sup>231</sup> As a result,

<sup>228</sup> Another possible interpretation of *Dombroski* was that its formulation of *Belvedere* was specifically applicable to the tort of insurer bad faith. See Jason Cummings, *Ohio Supreme Court Holds that Insurer's Alleged Bad Faith Insufficient to Pierce Corporate Veil to Holding Company*, MORRIS MANNING & MARTIN LLP (2007), <http://www.mmmlaw.com/industry/08Winter6.html> (noting that "under this modified version of the piercing the corporate veil test, an Ohio court likely will hold that an insurer's bad faith in denying a policyholder's claim is insufficient to pierce the corporate veil and hold the shareholders liable.").

<sup>229</sup> Part of this problem centers around the rules versus standard debate. While clear bright line rules permit parties to plan behavior with readily predictable outcomes, some bad conduct escapes coverage because of loopholes. Veil piercing is an archetypal standard: it leaves judges great discretion and flexibility but lacks predictability which ultimately decreases the utility of the corporate form. See generally, Thompson, *supra* note 2, at 1036.

<sup>230</sup> See Ohio Dept. of Taxation, Tax Data Series, Corporation Franchise Tax for Tax Year 2009, [http://tax.ohio.gov/divisions/communications/publications/annual\\_reports/2008\\_Annual\\_Report/documents/corporation\\_franchise\\_tax.pdf](http://tax.ohio.gov/divisions/communications/publications/annual_reports/2008_Annual_Report/documents/corporation_franchise_tax.pdf) (last visited Jan. 23, 2010).

<sup>231</sup> See Merit Brief for Amicus Curiae Ohio Council of Retail Merchants, Ohio Chamber of Commerce, The Ohio Chapter of the National Federation of Independent Businesses, and the Ohio Farm Bureau Federation Supporting Appellants at 1, *Dombroski v. WellPoint, Inc.*, 895 N.E.2d 538 (Ohio 2008). The estimate of 52,000 is conservative. Corporations with less than ten shareholders are equally vulnerable to veil piercing. Expanding to include the number of

over 52,000 individual shareholders in Ohio are potentially personally vulnerable to creditors.<sup>232</sup> The Ohio Supreme Court allowed most of those shareholders to sleep a little better thanks to the additional protection by *Dombroski*. But other than relaxing the sole shareholder's state of mind, what can businesses take away from the decision? Entrepreneurs know that the Ohio Supreme Court is concerned with reinforcing limited liability to give real protection to shareholders. But, it is unclear how much security the Ohio Supreme Court is willing to provide.<sup>233</sup> The uncertainty of the law leaves business planners in a pickle: those wishing to have the insulation of limited liability must decide whether to incur the transactional costs associated with incorporating while knowing that those costs may be in vain. In particular, this may be a significant decision for small business owners or corporations with a number of subsidiaries who wish to appropriately partition assets among riskier enterprises. The uncertainty from *Dombroski* will likely make business entities unwilling to expend the time and resources to incorporate when there is no certain benefit at the end of the day. The resulting increase in the cost of capital makes risky projects that have positive value difficult to fund.<sup>234</sup>

While this is not the ideal situation, corporations are not without solutions to avoid the issue altogether. The most controllable part of *Belvedere* is the first prong that requires control or domination of the corporate entity by the shareholder.<sup>235</sup> The basic rule is corporations and shareholders are separate entities under the law and should be treated accordingly. Officers and directors of corporations should be diligent in their attention to corporate formalities.<sup>236</sup> It is insufficient to simply file for

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corporations with ten or fewer shareholders would greatly inflate the number of shareholders vulnerable.

<sup>232</sup> *Id.*

<sup>233</sup> *Dombroski* came to the Ohio Supreme Court on a certified conflict from the Seventh District not a discretionary appeal, which means the Ohio Supreme Court did not affirmatively choose to take the case. Rather, the court was compelled to decide the issue. There was no affirmative decision by the court to take a proactive stance in this area. Short of a series of mandatory appeals hashing out the exact boundaries of veil piercing, it may be a while before the court provides further guidance on the issue.

<sup>234</sup> Easterbrook & Fischel, *supra* note 8, at 97. Business owners use subsidiaries to segregate riskier assets into an incorporated subsidiary which is owned wholly by a parent corporation. The parent enjoys the benefits of the subsidiary and is insulated from liability if the assets of the subsidiary are insufficient to cover any claims against the business. Robert B. Thompson, *Agency Law and Asset Partitioning*, 71 U. CIN. L. REV. 1321, 1324-25 (2003).

<sup>235</sup> *Belvedere Condominium Unit Owners' Ass'n. v. R.E. Roark Cos., Inc.*, 617 N.E.2d 1075, 1086 (Ohio 1993).

<sup>236</sup> Legal practitioners should be scrupulous with the formation of the corporation and be certain to follow all the requirements set forth in the Ohio Revised Code, Chapter 1701. *See* OHIO REV. CODE ANN. §§ 1701.04-13 (West 2009). Directors

incorporation without issuing shares or electing directors.<sup>237</sup> The corporation should have separate accounts from the shareholders.<sup>238</sup> Similarly, if a customer makes a payment to the business, the client should make the check out to the corporation and not a shareholder.<sup>239</sup> The corporation's property should not be diverted from corporate use for the personal benefit of the shareholder.<sup>240</sup> Corporations should not pay personal bills from the company ledger or corporate obligations with personal funds.<sup>241</sup> If the corporation is suffering from illiquidity and cannot pay obligations as they come due, deposit a personal check into the company bank account – never pay corporate obligations from personal accounts.<sup>242</sup> The corporation's financial officer should ensure these personal "loans" to the corporation are recorded in the company's financial records.

Avoiding fraud or illegality from *Belvedere's* second prong is a straightforward requirement: *shareholders should do not do anything illegal!*<sup>243</sup> However, misrepresentation is not as easy to predict or evade. Parties should make clear the precise terms of agreements. The corporations should ensure that the creditor is aware of which entities are responsible for payment. For example, the use of overt signage or forms that clearly and explicitly display the corporation's name and location eliminate any potential confusion.<sup>244</sup>

For firms with subsidiaries, rather than incurring the costs of incorporation with no certain benefit, the subsidiary may be incorporated as a limited liability company (LLC) instead of a corporation. A limited liability company functions like a corporation in terms of its debts and

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should be elected in accordance with OHIO REV. CODE ANN. § 1701.55 (West 2009). Board meeting should be held and minutes of those meetings maintained under OHIO REV. CODE ANN. § 1701.61 (West 2009).

<sup>237</sup> Teri Rasmussen, *Piercing the Corporate Veil – What It Means and How to Avoid It*, OHIO PRACTICAL BUS. LAW, Nov. 25, 2007, <http://www.ohiopracticalbusinesslaw.com/2007/11/articles/collections/piercing-the-corporate-veil-what-it-means-and-how-to-avoid-it/>.

<sup>238</sup> David B. Cathcart, Michael R. Tucci, & Jennifer E. Gross, *Avoid the Corporate Veil Getting Pierced – Protecting from Personal Liability for Corporate Obligations*, MANSOUR, GAVIN, GERLACK, & MANOS CO. L.P.A., Dec. 15, 2008, [http://www.mggmlpa.com/news\\_full\\_article.php?id=44&flag=news&from=archive&year=2008](http://www.mggmlpa.com/news_full_article.php?id=44&flag=news&from=archive&year=2008).

<sup>239</sup> *Id.*

<sup>240</sup> *Taylor Steel, Inc. v. Keeton*, 417 F.3d 598, 598 (6th Cir. 2005).

<sup>241</sup> Rasmussen, *supra* note 237.

<sup>242</sup> *Id.*

<sup>243</sup> *Belvedere Condominium Unit Owners' Ass'n. v. R.E. Roark Cos., Inc.*, 617 N.E.2d 1075, 1086 (Ohio 1993).

<sup>244</sup> Rasmussen, *supra* note 237.

obligations, but like a partnership for tax purposes.<sup>245</sup> Thus, LLCs enjoy the same limited liability status as a corporation<sup>246</sup> and LLC's veil may be pierced like any limited liability entity.<sup>247</sup> However, the transactional costs of that status are much lower. Corporations must maintain formalities, both at formation and as part of the continuing operations and management of the company. However, there are far fewer costs for an LLC since an LLC is easier to form and maintain.<sup>248</sup> These lower transactional costs justify the added protection of limited liability. While the veil of an LLC can still be pierced, the members incur fewer costs for protection and prevent parties from using the 'formalities' factor from the veil piercing test.<sup>249</sup> As a result, some corporations can take measures to add a layer of protection at a fraction of the cost.

Despite these practical safeguards, the issue of veil piercing can be a hand-wringing topic to the small business owner. The prospect of personal liability for the debts and obligations of the corporation is a risk no entrepreneur wants to run. The ability to run a business free and clear of personal liability is a tremendous benefit. Veil piercing should not be used as a tax on the unwary shareholder or the entrepreneur.<sup>250</sup> The law in Ohio has provided more security for the owners of small businesses through its recent decision in *Dombroski*. While not as clear as it could be, the *Belvedere* standard as modified in *Dombroski* does help secure limited liability for corporations with fewer shareholders and puts corporate law in Ohio in the right direction. Only time will tell if veil piercing in Ohio will solidify into a concrete and predictable rule which entrepreneurs can confidently rely.

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<sup>245</sup> *Dexxon Digital Storage, Inc. v. Haenszel*, 832 N.E.2d 62 (Ohio App. 5th Dist. 2005).

<sup>246</sup> OHIO REV. CODE ANN. § 1705.48(B) (West 2010) (members of an LLC are not personally liable for the debts of the company "solely by reason of being a member or manager of the limited liability company.").

<sup>247</sup> *Ruffing v. Masterbuilt Tool & Die, LLC*, No. 1:08-CV-01254, 2009 WL 185950, at \*16 (N.D. Ohio Jan. 23, 2009).

<sup>248</sup> Curtis J. Braukmann, *Limited Liability Companies*, 39 U. KAN. L. REV. 967, 992 (1991) (noting that "LLC[s] lack[] centralized management and operating under a statute requiring few formalities.").

<sup>249</sup> However, other factors may become more significant due to the general formalities. *Id.* Some states have dealt with this issue by passing statutes which remove formalities as a consideration for piercing the veil of an LLC. *See* CAL. CORP. CODE § 1702(c) (West 2010).

<sup>250</sup> Bainbridge, *supra* note 13, at 535.